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Circuits Split over Whether There Is Standing to Sue

IN THIS ISSUE

WINTER 2018 | VOLUME 43 NUMBER 2

FEATURES

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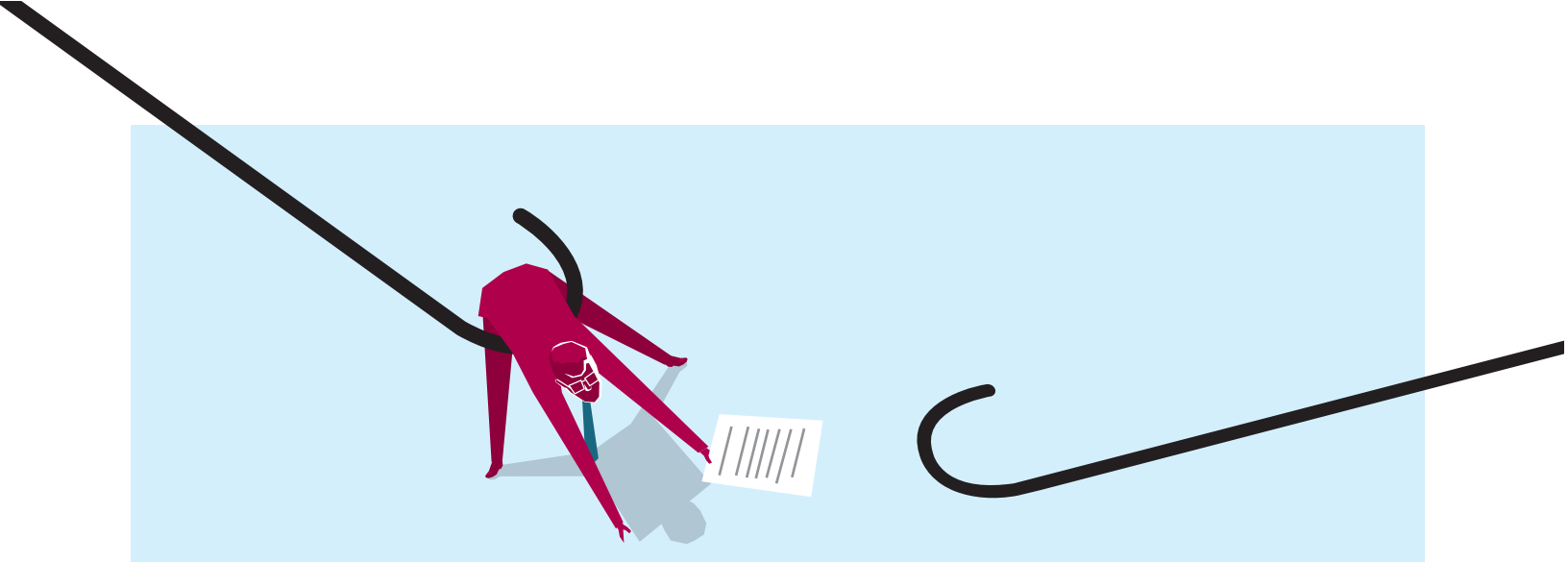
COLUMNS

DEPARTMENTS



New Test for Forum Selection Clauses

By Matthew S. Mulqueen, Litigation News *Associate Editor*

One of the first issues litigants face in multiparty litigation is whether the plaintiff filed the case in the appropriate forum. This question can quickly become complicated when some, but not all, of the parties are subject to a forum selection clause. In *In re Howmedica Osteonics Corp.*, the U.S. Court of Appeals for the Third Circuit tackled the problem by establishing a new test for situations where both contracting and noncontracting parties are found in the same case. Although the new test is not flawless, it seeks to harmonize the competing private and public interests that govern such cases, say ABA Section of Litigation leaders.

SUIT AND TRANSFER

The litigants' dispute arose out of a soured employment relationship. Several California sales representatives of a New Jersey orthopedic supplier grew dissatisfied with their employer and decided to strike out as independent contractors for a competitor. Several of the representatives' customers followed them to the competitor. Suspecting that the representatives had improperly solicited the customers before their departure, the orthopedic supplier brought suit in the U.S. District Court for the District of New Jersey against the representatives and its competitor. The supplier also joined the competitor's California distributor as a necessary party under Federal Rule of Civil Procedure 19(b).

The defendants jointly moved to transfer the case to the U.S. District Court for the Northern District of California pursuant to 28 U.S.C. § 1404(a), which, for "the convenience of parties and witnesses" and "in the interest of justice," allows transfer to a district where the case "might have been brought." The distributor further argued that the New Jersey court lacked jurisdiction over it. The orthopedic supplier objected to the transfer request, noting that the representatives had all signed confidentiality and non-compete agreements during their employment that contained forum selection clauses. The clauses designated New Jersey (or, in one representative's case, Michigan) as the forum for any litigation arising out of the agreements.

The district court granted the defendants' motion and transferred the case to the Northern District of California. Following the transfer, the orthopaedic supplier petitioned the Third Circuit for a writ of mandamus. The supplier asked the appellate court to vacate the district court's transfer order on the ground that it conflicted with the U.S. Supreme Court's decision in *Atlantic Marine Construction Co. v. U.S. District Court for the Western District of Texas*, which held that, except in "the most unusual cases," a district court should give effect to a valid forum selection clause. The court of appeals granted the mandamus petition.

FORUM SELECTION UNDER *ATLANTIC MARINE*

In cases without a forum selection clause, courts apply a balancing test to transfer requests. The test typically weighs private interests, including the convenience of the parties and witnesses and the location of relevant evidence, with public interests, including the relative congestion in the two potential fora and the familiarity of the judge with applicable state law in diversity cases.

The weighing of private and public interests changes when a forum selection clause enters the picture. In *Atlantic Marine*, the Supreme Court made clear that, in most cases, district courts must enforce valid forum selection clauses when adjudicating section 1404(a) transfer motions. However, the Court did not address how that general rule should

apply where noncontracting parties are present or where there are competing forum selection clauses, personal jurisdiction challenges, or allegations of necessary party status.

All of those complicating factors were squarely before the Third Circuit. The appellate court decided that it needed a fresh framework to determine how forum selection clauses affect the section 1404(a) transfer analysis where both contracting and noncontracting parties are found in the same case and where the noncontracting parties' private interests run headlong into the presumption of *Atlantic Marine*.

NEW FOUR-STEP INQUIRY

The Third Circuit devised a four-step inquiry to aid its analysis. The Third Circuit concluded that when faced with a situation like the one in the case before it, courts should perform the following tasks: First, the court should assume that *Atlantic Marine* applies to parties who agreed to forum selection clauses and that, "[i]n all but the most unusual cases," claims concerning those parties should be litigated in the fora designated by the clauses. Second, the court should perform an independent analysis of private and public interests relevant to noncontracting parties, just as when adjudicating a section 1404(a) transfer motion involving those parties in the absence of any forum selection clauses.

If the first two steps point in separate directions, the court should take the third step of considering severing claims under Rule 21. Fourth, the court should exercise its discretion in choosing the most appropriate course of action, measuring its decision against efficiency interests in avoiding duplicative litigation, the noncontracting parties' private interests, and any prejudice that a particular transfer decision would cause with respect to those interests.

4-STEP INQUIRY

1. Litigate claims in the fora designated by any applicable forum selection clauses.
2. Analyze private and public interests relevant to non-contracting parties.
3. If the first two steps point in separate directions, consider severing claims.
4. Choose the most appropriate course of action, measuring its decision against efficiency interests, the non-contracting parties' private interests, and any prejudice that a transfer decision would cause.

REVERSAL AND SEVERANCE

Applying this test to the facts before it, the Third Circuit concluded that the district court erred in transferring the entire case to California. The appellate court began with the presumption that the New Jersey forum selection clauses were enforceable against the sales representatives. The court then concluded that both public and private interests weighed in favor of transferring the claims against the noncontracting defendants to California.

Under the third prong of its test, the court found that the noncontracting parties could properly be severed from the action because the distributor was not a "necessary party" within the meaning of Rule 19(b) and was not subject to personal jurisdiction in New Jersey. Finally, under the fourth step of its inquiry, the court weighed the noncontracting parties' interests in efficiency and concluded that the burden of litigating in two fora was insufficient to outweigh enforcement of the forum selection clauses. The court therefore severed the case and transferred the claims against the competitor and distributor to the Northern District of California.

MAINTAINING EFFICIENCY IN MULTIPLE FORA

Severing claims in order to enforce forum selection clauses is unlikely to leave all parties happy. "This appears to be one of those cases in which there is no perfect answer, in that the most 'efficient' result of complete transfer of the case to California (which the district court opted to do) also happens to do violence to the contractually agreed outcome amongst most of the parties," says Robert J. Will, St. Louis, MO, cochair of the Section of Litigation's Pretrial Practice & Discovery Committee.

In its opinion, the appellate court suggested that the problems inherent in multi-fora litigation could be addressed through common pretrial procedures, video depositions, stipulations, and any similar tools used by judges in cases managed pursuant to multidistrict litigation statutes. While that "sounds feasible," the real effect of such mechanisms "probably will depend on how much the lawyers litigating the matters can agree on procedures to minimize duplication of effort," says Kenneth M. Klemm, New Orleans, LA, cochair of the Section's Pretrial Practice & Discovery Committee.

"It seems unlikely that federal judges in different districts will modify their usual pretrial procedures or otherwise coordinate on litigation pending in two different districts when not required to do so," predicts Klemm. "On the other hand, severance does provide courts with an avenue to ensure enforcement of forum selection clauses negotiated between parties, and the Rule 19 inquiry assists somewhat to solve the risk of duplicative litigation," he notes.

Ultimately, the Third Circuit's opinion may "have little effect on parties' use of forum selection clauses, since one cannot bind nonsigners to such a clause, and in cases such as this, nonsigner parties may be unavoidable," believes Will. Nevertheless, "the decision should provide confidence to parties using forum selection that these clauses will be enforced unless the public policy of a particular forum prohibits enforcement," Klemm concludes.

RESOURCES

- *In re Howmedica Osteonics Corp.*, 867 F.3d 390 (3d Cir. 2017), available at http://bit.ly/LN432-howmedica.
- Fed. R. Civ. P. 19, available at http://bit.ly/LN432-frcp19.
- *In re Rolls Royce Corp.*, 775 F.3d 671 (5th Cir. 2014), available at http://bit.ly/LN432-rolls-royce.
- *Atl. Marine Constr. Co. v. U.S. Dist. Court for W. Dist. of Tex.*, 134 S. Ct. 568 (2013), available at http://bit.ly/LN432-marine.
- 28 U.S.C. § 1404(a), available at http://bit.ly/LN432-usc1404
- Fed. R. Civ. P. 21, available at http://bit.ly/LN432-frcp21.
- 2015 Amendments to the Federal Rules of Civil Procedure, available at http://bit.ly/LN432-2015amend.
- James H. Bowhay, "Checklist for Motions to Transfer Pursuant to a Forum Selection Clause," *Com. & Bus. Litig.*, Mar. 17, 2017, available at http://bit.ly/LN432-bowhay.
- Lauren M. Gregory, "Amended Federal Rules Emphasize Early Case Assessment," *Litigation News*, Apr. 4, 2016, available at http://bit.ly/LN432-gregory.